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DOCUMENT CONTROL

LARRY J. WEATHERS  
DIRECT (206) 628-7161  
larryweathers@dwtt.com

2600 CENTURY SQUARE  
1501 FOURTH AVENUE  
SEATTLE, WA 98101-1688

TEL (206) 622-3150  
FAX (206) 628-7699  
www.dwt.com

January 8, 2001

Arizona Corporation Commission  
**DOCKETED**

JAN 09 2001

Arizona Corporation Commission  
Docket Control-Utilities Division  
1200 West Washington  
Phoenix, AZ 85007

DOCKETED BY	
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Re: ACC Docket No. T-01051B-99-0105

Dear Docket Control:

Enclosed for filing are the original and 10 copies of *AT&T's Reply to Price Cap Plan Revisions of Staff and Qwest* in the above named docket. An electronic copy of the brief will be sent via e-mail to the e-mail service list on Tuesday, January 9, 2001. Please call me if there are any questions concerning this filing.

Very truly yours,

Davis Wright Tremaine LLP

Larry J. Weathers  
Paralegal

Enclosures

cc: Rick Wolters  
Mary Tribby  
Mark Trierweiler  
Mary Steele

BEFORE THE ARIZONA CORPORATION COMMISSION

CARL J. KUNASEK

Chairman

JIM IRVIN

Commissioner

WILLIAM A. MUNDELL

Commissioner

IN THE MATTER OF THE APPLICATION OF )  
U S WEST COMMUNICATIONS, INC., A )  
COLORADO CORPORATION, FOR A )  
HEARING TO DETERMINE THE EARNINGS )  
OF THE COMPANY, THE FAIR VALUE OF )  
THE COMPANY FOR RATEMAKING )  
PURPOSES, TO FIX A JUST AND )  
REASONABLE RATE OF RETURN )  
THEREON AND TO APPROVE RATE )  
SCHEDULES DESIGNED TO DEVELOP )  
SUCH RETURN. )

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DOCKET NO. T-01051B-99-0105

**AT&T'S REPLY TO PRICE CAP  
PLAN REVISIONS OF STAFF AND  
QWEST**

**I. INTRODUCTION**

Qwest and Staff have now proposed a revised Price Cap Plan and Settlement Agreement incorporating a few of the changes proposed by the parties to this proceeding. The agreed revisions, however, are superficial and fail to address the significant concerns raised by the parties. For this reason, AT&T of the Mountain States, Inc. ("AT&T") continues to request that the Commission reject the proposed settlement.

**II. DISCUSSION**

AT&T has previously identified nine major problems with the Price Cap Plan as set forth below:

- 1. The Proposed Revenue Requirement is Too High:** Because the revenue requirement established by the Price Cap Plan is overstated, the approved Qwest prices

going into the Plan are too high, to the detriment of Arizona consumers.

**2. The Proposed Productivity Factor is Too Low:** The Plan fails to share with consumers gains that Qwest is likely to experience because the productivity factor is set too low and because the productivity calculation fails to consider gains in productivity that are likely to occur during the term of the Plan.

**3. Switched Access Rates Remain Substantially Above Cost:** The Plan injures consumers because it fails to reduce Qwest's charges for switched access to a competitive level, ensuring that intraLATA toll rates will remain substantially higher than they would be in a competitive market.

**4. New Services and Packages Automatically Receive Pricing Flexibility:** The Plan circumvents existing Commission rules by giving Qwest flexible pricing for any new service and for any service presently classified as non-competitive simply by offering the service in a package with a competitive service. This effectively grants Qwest pricing flexibility for all existing services.

**5. Qwest's Ability to Spot Price Undercuts Competition:** In combination with the ability to obtain flexible pricing for any service, the Plan also undercuts competition by permitting Qwest to engage in "spot" pricing. The Plan permits Qwest to offer different packages and different prices in any geographic area chosen by Qwest. This permits Qwest to undercut prices of services offered by competitors in the limited geographic areas where Qwest faces competition while maintaining or increasing its profit margin in other areas.

**6. The Plan Does not Adequately Define the Price Floors for Basket 3 Services:** The Plan fails to establish the price floors for services in Basket 3, exacerbating the potential for anti-competitive pricing on the part of Qwest.

**7. Insufficient Notice and Opportunity for Commission Review:** The proposed

Plan does not allow competitors or the Commission sufficient opportunity to review Qwest's pricing proposals.

**8. The Agreement Is Riddled with Errors and Ambiguities:** There are miscellaneous errors and ambiguities in both the Plan and the Settlement Agreement that provide a potential for misunderstanding and litigation that will burden the Commission and the competitive process, all to the ultimate detriment of Arizona consumers.

Of these eight significant problems, the changes now proposed address only the last. Staff and Qwest have eliminated some of the more minor ambiguities and errors in the Plan. Qwest and Staff have made no more than a passing effort, however, to address the substantive problems that make the Price Cap Plan contrary to the public interest.

In its newly proposed revisions, Staff and Qwest make no changes to the sections of the Plan that address the revenue requirement (problem 1), the productivity factor (problem 2), switched access rates (problem 3), Qwest's ability to spot price (problem 5) or the lack of notice that is permitted under the Plan for actions that may harm competitors (problem 7). AT&T has explained in detail in its post-hearing brief why these problems create substantial harm to the public and to the state of competition in Arizona.

Qwest and Staff have made minor revisions to the sections of the Plan that deal with pricing flexibility for new services and packages (problem 4) and the price floors for Basket 3 services (problem 6). These superficial changes, however, do not eliminate the concerns raised AT&T regarding these provisions of the Plan.

Paragraph 4(e) of the Plan gives Qwest's the ability to obtain flexible pricing for new services without demonstrating the extent to which those services actually face competition. The provision also gives Qwest the ability to obtain pricing flexibility for noncompetitive services by offering those services as a "new package." AT&T and other parties objected to this provision on the basis that it effectively grants Qwest pricing flexibility for all services without the

necessity of compliance with existing Commission rule R14-1108.

Staff and Qwest have now added language to Paragraph 4(e) to the effect that "the Commission retains the right to object to any proposed classification or filing." This addition adds no substantive protections for consumers or competitors. The Commission always has the right to reject proposed classifications. This provision of the Price Cap Plan, however, removes the Commission's ability to rely on the standards provided by R14-1108 in evaluating Qwest's proposals. Nothing about the revision to Paragraph 4(e) solves the concern that Qwest may obtain pricing flexibility for existing services without showing that it in fact faces competition in providing those services.

Qwest and Staff have made no changes to Paragraph 4(g) of the Plan that permits Qwest to offer new services and packages "to select customer groups based on their purchasing patterns and geographic locations, for example." As AT&T pointed out in its post-hearing briefing, this provision, when combined with the provisions of 4(e) allowing flexible pricing for monopoly services, provides Qwest with an effective tool to prevent competition from developing in Arizona.

The failure of Staff and Qwest to agree on price floors for flexibly priced services in Basket 3 exacerbates this problem. In response, Qwest and Staff have clarified that Qwest will be subject to imputation requirements in establishing Basket 3 pricing. The problem, however, is that Qwest and Staff have failed to clarify how those imputation rules will be applied. As AT&T pointed out in its post-hearing briefing, and as became clear at the hearing, Qwest and Staff have very different views on what must be imputed into the price floor for Basket 3 services. Under Qwest's interpretation of the imputation rules, Qwest retains the ability to significantly under-price competitors in limited geographic areas in order to destroy any threat of competition. The Plan's failure to clarify how imputation rules will be applied continues to create the risk of significant harm to competitors if the Plan is adopted.

### III. CONCLUSION

For all these reasons, AT&T requests and the reasons set forth in AT&T's post-hearing brief that the Commission reject the proposed Settlement Agreement and Price Cap Plan.

DATED this 31<sup>st</sup> day of January, 2001.

**AT&T COMMUNICATIONS OF THE  
MOUNTAIN STATES, INC.**

By: Mary B. Tribby  
Mary B. Tribby  
Richard S. Wolters  
1875 Lawrence Street, #1500  
Denver, Colorado 80202  
303-298-6741 Phone  
303-298-6301 Facsimile  
rwolters@att.com E-mail

Mary E. Steele  
DAVIS WRIGHT TREMAINE LLP  
1501 Fourth Avenue  
2600 Century Square  
Seattle, WA 98101-1688  
206-628-7772  
206-628-7699 (Facsimile)

**CERTIFICATE OF SERVICE**  
**ACC Docket No. T-01051B-99-0105**

I hereby certify that I have on this 8<sup>th</sup> day of January 2001 delivered the original and 10 copies of *AT&T's Reply to Price Cap Plan Revisions of Staff and Qwest* via FedEx next business morning service to:

Docket Control – Utilities Division  
Arizona Corporation Commission  
1200 West Washington  
Phoenix, Arizona 85007

Jane Rodda  
Acting Chief Administrative Law Judge  
Hearing Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

Maureen Scott  
Arizona Corporation Commission  
Legal Division  
1200 West Washington Street  
Phoenix, AZ 85007

Christopher Kempley  
Arizona Corporation Commission  
Legal Division  
1200 West Washington Street  
Phoenix, AZ 85007

Timothy Berg  
Theresa Dwyer  
Fennemore Craig, P.C.  
3003 North Central, Suite 2600  
Phoenix, AZ 85012

Deborah Scott  
Director – Utilities Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

Lyn Farmer, Esq.  
Legal Division  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

And on the same day a copy of the foregoing was sent via U.S. Mail, postage prepaid, to:

Carl J. Kunasek, Chairman  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

James M. Irvin, Commissioner  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

William Mundell, Commissioner  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

Scott S. Wakefield  
Chief Counsel  
RUCO  
2828 North Central Avenue, Suite 1200  
Phoenix, AZ 85004-1022

Jerry Porter  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

Hercules Alexander Dellas  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

Chuck Turner, Mayor  
Town of Gila Bend  
P. O. Box A  
644 W. Pima Street  
Gila Bend, AZ 85337-0019

Michael W. Patten  
Brown & Bain, P.A.  
2901 North Central Avenue, Suite 2000  
Phoenix, AZ 85012

Darren S. Weingard  
Natalie D. Wales, Attorney  
Sprint Communications Company L.P.  
1850 Gateway Drive, 7<sup>th</sup> Floor  
San Mateo, CA 94404-2467

Raymond S. Heyman  
Randall H. Warner \*  
Roshka Heyman & Dewulf PLC  
Two Arizona Center  
400 North 5th Street, Suite 1000  
Phoenix, AZ 85004

Thomas F. Dixon  
WorldCom, Inc.  
707 17th Street, Suite 3900  
Denver, CO 80202

Jim Scheltema  
Blumenfeld & Cohen  
1625 Massachusetts Ave N.W., Suite 300  
Washington, DC 20036

Patrick Black  
Arizona Corporation Commission  
1200 West Washington Street  
Phoenix, AZ 85007

Jon Poston  
6733 East Dale Lane  
Cave Creek, AZ 85331

Steven J. Duffy  
Ridge & Isaacson, P.C.  
3101 North Central Avenue, Suite 432  
Phoenix, AZ 85012

Joan S. Burke  
Osborn, Maledon PA  
2929 N. Central Ave., 21st Floor  
P. O. Box 36379  
Phoenix AZ 85012-2794

Richard Lee  
Snively, King & Majoros  
O'Connor & Lee, Inc.  
1220 L. Street, N. W., Suite 410  
Washington, DC 20005

Peter Q. Nyce  
General Attorney, Regulatory Law Office  
U. S. Army Legal Services Agency  
Department of the Army  
901 N. Stuart Street, Suite 700  
Arlington, VA 22203-1837

Douglas Hsiao  
Rhythm Links, Inc.  
6933 Revere Parkway  
Englewood, CO 80112

Jeffrey W. Crockett  
Snell & Wilmer  
One Arizona Center  
Phoenix, AZ 85004-0001

Martin A. Aronson  
William D. Cleaveland  
Morrill & Aronson, P.L.C.  
One East Camelback, Suite 340  
Phoenix, AZ 85012-1648

Thomas H. Campbell  
Lewis and Roca  
40 North Central Avenue  
Phoenix, AZ 85004

Albert Sterman  
Arizona Consumers Council  
2849 E. 8th Street  
Tucson, AZ 85716

William F. Cottrell  
7064 W. Angela Dr.  
Glendale, AZ 85308

Mark N. Rogers  
Excell Agent Services, L.L.C.  
2175 W. 14<sup>th</sup> Street  
Tempe, AZ 85281

Diane Bacon, Legislative Director  
Communications Workers of America  
District 7 AFL-CIO, CLC  
5818 N. 7<sup>th</sup> Street, Suite 206  
Phoenix, AZ 85014-5811

Dated this 8 January 2001

By Ramy Julkathars